Supreme Court, U.S.
FILED
DEC 29 1995
CLERK

No. 95-713

In the Supreme Court of the United States

OCTOBER TERM, 1995

QANTAS AIRWAYS LIMITED, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

DREW S. DAYS, III
Solicitor General
LORETTA C. ARGRETT
Assistant Attorney General
BRUCE R. ELLISEN
THOMAS J. CLARK
Attorneys
Department of Justice
Washington, D.C. 20530
(202) 514-2217

QUESTION PRESENTED

Former Section 892 of the Internal Revenue Code, as in effect prior to 1986, 26 U.S.C. 892 (1982), granted an exemption from income taxation to "foreign governments." Neither that Section nor any other provision of the Code then defined that term.[1] The question presented is whether the Treasury reasonably interpreted the term "foreign governments" in that former Section of the Code to mean "integral parts or controlled entities of a foreign sovereign to the extent not engaged in commercial activities in the United States" (26 C.F.R. 1.892-1 (1982)).

---

[1] Section 892 was amended in 1986 by Section 1247(a) of the Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 2583, and further amended in 1988 by Section 1012(t) of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. No. 100-647, 102 Stat. 3572. See App., *infra*, 1a-2a; page 2, *infra*.

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Statement	2
Argument	4
Conclusion	6
Appendix	1a

TABLE OF AUTHORITIES

Cases:

Alfred Dunhill of London, Inc. v. *Republic of Cuba*, 425 U.S. 682 (1976)	5
Bank of the United States v. *Planters' Bank of Georgia*, 22 U.S. (9 Wheat.) 904 (1824)	4
Cottage Savings Ass'n v. *Commissioner*, 499 U.S. 554 (1991)	5
National Muffler Dealers Ass'n v. *United States*, 440 U.S. 472 (1979)	5
Republic of Argentina v. *Weltover, Inc.*, 504 U.S. 607 (1992)	5
The "Gul Djemal", 264 U.S. 90 (1924)	4, 5
United States v. *Correll*, 389 U.S. 299 (1967)	5-6

Statutes and regulation:

Foreign Sovereign Immunities Act of 1976, 28 U.S.C. 1602-1611	5
28 U.S.C. 1605(a)(2)	5
Internal Revenue Code (26 U.S.C.) (1982):	
§ 892	2, 3, 4, 5, 6, 1a
§ 892(a)(2)(B)	5, 1a-2a
26 C.F.R. 1.892-1(b) (1982)	3

In the Supreme Court of the United States

OCTOBER TERM, 1995

No. 95-713

QANTAS AIRWAYS LIMITED, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1-11) is reported at 62 F.3d 385. The Court of Federal Claims issued two opinions. The first (Pet. App. 42-56) is unreported. The second (Pet. App. 12-41) is reported at 30 Fed. Cl. 851.

JURISDICTION

The judgment of the court of appeals was entered on August 3, 1995. The petition for a writ of certiorari was filed on November 1, 1995. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioner is an Australian corporation that operates an international airline. The stock of petitioner is wholly owned by the Australian government. The income from petitioner's operations thus inures ultimately to the benefit of the Australian government (Pet. App. 2-3).

Petitioner maintains a regional office in a building that it owns in San Francisco, California. During the tax years involved in this case (1983-1985), petitioner occupied only three floors of that building. The remaining floor space was rented at market rates (Pet. App. 3). Petitioner also owned 25 residential properties in a suburb of San Francisco. During the years in question, petitioner received capital gains from the sale of several of those properties and received rental income by leasing the others (*ibid.*).

2. On its federal income tax returns for these taxable years, petitioner reported as income the rents and capital gains it received in connection with the office and residential properties. Petitioner later filed amended income tax returns for all three years, however, claiming that this income was exempt from taxation under the then-applicable provisions of Section 892 of the Internal Revenue Code, 26 U.S.C. 892 (1982). See note 1, *supra*. Petitioner asserted that it was therefore entitled to a refund of the taxes that it paid on that income. When the refund claims were not allowed by the Internal Revenue Service, petitioner commenced this refund suit in the Court of Federal Claims (Pet. App. 3-4).

3. Petitioner moved for summary judgment, contending that its income was exempt from tax under 26 U.S.C. 892 (1982) because petitioner was a "foreign

government." The court denied the motion, explaining that a commercial airline "is not, in the usual sense, a foreign government" (Pet. App. 4, 47). The court noted (*id.* at 4, 52-53) that applicable Treasury regulations interpreted the term "foreign government" to exclude "integral parts" and "controlled entities" of foreign sovereigns that are "engaged in commercial activities in the United States" (26 C.F.R. 1.892-1(b) (1982)). Because the parties had agreed that petitioner was a "controlled entity" of a foreign sovereign (Pet. App. 7), the court scheduled a trial to determine whether the income in question was from "commercial activities in the United States."

After trial, the Court of Federal Claims reversed its prior legal ruling. The court held that petitioner qualified as a "foreign government" under Section 892 solely because it was a controlled entity of a foreign sovereign. The court noted that "[i]t is true that Congress ultimately decided in 1986 to codify the portions of Treas. Reg. 1.892 that excepted from the foreign government exception income derived from commercial sources" (Pet. App. 40). But the court concluded that the statutory language that was applicable to years before 1986 did not permit that interpretation (*ibid.*). Because this case arose during the years when the former provisions of Section 892 were in effect, the court concluded that petitioner's commercial income was exempt from tax (Pet. App. 41).

4. The court of appeals reversed (Pet. App. 1-11). The court observed that, prior to 1986, Congress had not defined the term "foreign government" in Section 892 and that the legislative history shed no light on its proper scope (Pet. App. 6). Because the term

"foreign government" as used in Section 892 was capable of more than one definition, the court concluded that the definition adopted by the Treasury regulation should be sustained if it is reasonable and not inconsistent with the statute (Pet. App. 5-9). The court held that the Treasury's regulatory definition was reasonable because the "commercial activities" of a "controlled entitity"—such as activities conducted by "a corporation that exists solely to operate an international airline that competes with private ones" (*id.* at 8)—are not inherently governmental activities (*ibid.*).

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court of appeals. Further review is therefore not warranted.

1. Section 892 of the Internal Revenue Code, as in effect prior to 1986 (see note 1, *supra*), exempted "[t]he income of foreign governments" from taxation. The term "foreign governments" was not then defined in the Code. Historically, however, that term ordinarily referred to a government acting in its sovereign capacity and not as a participant in a commercial enterprise. See *Bank of the United States* v. *Planters' Bank of Georgia*, 22 U.S. (9 Wheat.) 904, 907 (1824) (Marshall, C.J.). For example, in a decision that was contemporaneous with the original enactment of Section 892, this Court held in *The "Gul Djemal"*, 264 U.S. 90 (1924), that a ship that was owned and manned by the Government of Turkey and that was commanded by a commissioned officer of the Turkish Navy, but that had been chartered to carry passengers and goods for hire, could not claim

immunity in a court of the United States from a libel by an unpaid supplier because it was engaged at the time in a commercial activity. *Id.* at 95.

As discussed in *Alfred Dunhill of London, Inc.* v. *Republic of Cuba*, 425 U.S. 682, 695-706 (1976), this Court has frequently differentiated between states—both domestic and foreign—acting in their governmental and commercial capacities. That same distinction was drawn clearly by Congress in the Foreign Sovereign Immunities Act of 1976, 28 U.S.C. 1602-1611. Contrary to petitioner's suggestion (Pet. 26), that Act explicitly denies sovereign immunity to an agency or instrumentality of a "foreign state" that is engaged in "commercial activity" (28 U.S.C. 1605(a)(2)). See also 28 U.S.C. 1603(a); *Republic of Argentina* v. *Weltover, Inc.*, 504 U.S. 607, 610-620 (1992). Moreover, in amending Section 892 of the Internal Revenue Code in 1986, Congress expressly incorporated this long-standing distinction by providing specifically that the income of controlled entities of foreign sovereigns engaged in commercial activities is subject to tax. 26 U.S.C. 892 (a)(2)(B).

The 1986 amendment to Section 892 thus expressly incorporates the same reasonable interpretation of the term "foreign government" that the Treasury had adopted in regulations issued under the former statute. In concluding that the Treasury's reasonable interpretation of this statutory term is entitled to deference and should therefore be sustained (Pet. App. 5-8), the court of appeals plainly did not depart from the precedent of this Court or of any other court of appeals. See, *e.g.*, *Cottage Savings Ass'n* v. *Commissioner*, 499 U.S. 554, 560-561 (1991); *National Muffler Dealers Ass'n* v. *United States*, 440 U.S. 472, 476 (1979); *United States* v. *Correll*, 389 U.S. 299, 307

(1967). As the court of appeals held, the Treasury's regulations reasonably concluded that, "to the extent controlled entities are engaged in commercial activities in the United States, they are not treated as a part of a foreign government within the meaning of [Section] 892" (Pet. App. 10).

2. The question of the proper scope of the former provisions of Section 892 of the Internal Revenue Code lacks any recurring importance. For all tax years after 1985, the amended provisions of that Section apply and, under those provisions, petitioner concedes (Pet. 20) that all entities controlled by foreign sovereigns that engage in commercial activities within the United States are subject to tax. See 26 U.S.C. 892; Pet. App. 37; App., *infra*, 1a-2a. Further review of the proper scope of the pre-1986 version of this statute is therefore not warranted.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

DREW S. DAYS, III
Solicitor General
LORETTA C. ARGRETT
Assistant Attorney General
BRUCE R. ELLISEN
THOMAS J. CLARK
Attorneys

DECEMBER 1995

APPENDIX

Section 892 of the Internal Revenue Code, 26 U.S.C. 892, as amended by Section 1012(t) of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. No. 100-647, 102 Stat. 3527, provides:

INCOME OF FOREIGN GOVERNMENTS AND OF INTERNATIONAL ORGANIZATIONS

(a) Foreign Governments—

(1) In general—

The income of foreign governments received from—

(A) investments in the United States in—

(i) stocks, bonds, or other domestic securities owned by such foreign governments, or

(ii) financial instruments held in the execution of governmental financial or monetary policy, or

(B) interest on deposits in banks in the United States of moneys belonging to such foreign governments,

shall not be included in gross income and shall be exempt from taxation under this subtitle.

(2) Income received directly or indirectly from commercial activities—

(A) In general—

Paragraph (1) shall not apply to any income—

(i) derived from the conduct of any commercial activity (whether within or outside the United States),

(ii) received by a controlled commercial entity or received (directly or indirectly) from a controlled commercial entity, or

(iii) derived from the disposition of any interest in a controlled commercial entity.

(B) Controlled commercial entity—

For purposes of subparagraph (A), the term "controlled commercial entity" means any entity engaged in commercial activities (whether within or outside the United States) if the government—

(i) holds (directly or indirectly) any interest in such entity which (by value or voting interest) is 50 percent or more of the total of such interests in such entity, or

(ii) holds (directly or indirectly) any other interest in such entity which provides the foreign government with effective control of such entity.

For purposes of the preceding sentence, a central bank of issue shall be treated as a controlled commercial entity only if engaged in commercial activities within the United States.

* * * * *